8 8

Nos. 93-1612 and 93-1613

In the Supreme Court of the United States

OCTOBER TERM, 1994

NATIONSBANK OF NORTH CAROLINA, N.A., ET AL.,
PETITIONERS

v.

VARIABLE ANNUITY LIFE INSURANCE COMPANY, ET AL.

EUGENE LUDWIG, COMPTROLLER OF THE
CURRENCY, ET AL., PETITIONERS

v.

VARIABLE ANNUITY LIFE INSURANCE COMPANY, ET AL.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

BRIEF FOR THE FEDERAL PETITIONERS

DREW S. DAYS, III
Solicitor General

FRANK W. HUNGER
Assistant Attorney General

PAUL BENDER
Deputy Solicitor General

EDWARD C. DUMONT
Assistant to the Solicitor General

MARK B. STERN
JACOB M. LEWIS
Attorneys

Department of Justice
Washington, D.C. 20530
(202) 514-2217

JULIE L. WILLIAMS
Chief Counsel

L. ROBERT GRIFFIN
ROSA M. KOPPEL
YVONNE D. MCINTIRE
Attorneys

Office of the Comptroller
of the Currency
Washington, D.C. 20219
(202) 874-5200

QUESTION PRESENTED

Whether federal law permits national banks, wherever located, to act as agents in the sale of annuities.

PARTIES TO THE PROCEEDINGS

In addition to the parties identified in the captions, the parties in the court of appeals included the United States, the Office of the Comptroller of the Currency, and NCNB National Bank of North Carolina and NCNB Securities, Inc. (the corporate predecessors of petitioners NationsBank of North Carolina, N.A., and NationsBanc Securities, Inc.).

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases—Continued: Page

Cases—Continued: Page

Statutes and regulation:

Miscellaneous:

In the Supreme Court of the United States

OCTOBER TERM, 1994

No. 93-1612

NATIONSBANK OF NORTH CAROLINA, N.A., ET AL., PETITIONERS

v.

VARIABLE ANNUITY LIFE INSURANCE COMPANY, ET AL.

No. 93-1613

EUGENE LUDWIG, COMPTROLLER OF THE CURRENCY, ET AL., PETITIONERS

v.

VARIABLE ANNUITY LIFE INSURANCE COMPANY, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE FEDERAL PETITIONERS

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-17a)[1] is reported at 998 F.2d 1295. That court's order denying rehearing and rehearing en banc, and

---

[1] "Pet. App." refers to the appendix to the petition in No. 93-1612.

the opinion dissenting therefrom (Pet. App. 18a-28a), are reported at 13 F.3d 833. The opinion of the district court (Pet. App. 29a-34a) is reported at 786 F. Supp. 639. The approval letter of the Office of the Comptroller of the Currency (Pet. App. 35a-48a) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on August 26, 1993. A petition for rehearing was denied on January 13, 1994. Pet. App. 18a-19a. The petitions for certiorari were filed on April 13, 1994, and were granted on June 6, 1994. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

STATUTORY PROVISIONS INVOLVED

1. Section 5136 of the Revised Statutes of 1878, 12 U.S.C. 24, as amended, provides in pertinent part as follows:

> Upon duly making and filing articles of association and an organization certificate a national banking association shall become, as from the date of the execution of its organization certificate, a body corporate, and as such, and in the name designated in the organization certificate, it shall have power—
>
> * * * * *
>
> Seventh. To exercise by its board of directors or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money

on personal security; and by obtaining, issuing, and circulating notes according to the provisions of title 62 of the Revised Statutes. The business of dealing in securities and stock by the association shall be limited to purchasing and selling such securities and stock without recourse, solely upon the order, and for the account of, customers, and in no case for its own account, and the association shall not underwrite any issue of securities or stock[.]

2. Section 13, para. 9, of the Federal Reserve Act, Act of Dec. 23, 1913, ch. 6, 38 Stat. 263, 12 U.S.C. 92 (Supp. V 1993), provides as follows:

In addition to the powers now vested by law in national banking associations organized under the laws of the United States any such association located and doing business in any place the population of which does not exceed five thousand inhabitants, as shown by the last preceding decennial census, may, under such rules and regulations as may be prescribed by the Comptroller of the Currency, act as the agent for any fire, life, or other insurance company authorized by the authorities of the State in which said bank is located to do business in said State, by soliciting and selling insurance and collecting premiums on policies issued by such company; and may receive for services so rendered such fees or commissions as may be agreed upon between the said association and the insurance company for which it may act as agent: *Provided, however*, That no such bank shall in any case assume or guarantee the payment of any premium on insurance policies issued through its agency by its principal: *And provided further*, That the bank shall not guarantee the truth

of any statement made by an assured in filing his application for insurance.

STATEMENT

1. This litigation involves a challenge to the Comptroller of the Currency's approval of an application by the corporate predecessors of petitioners NationsBank of North Carolina, N.A. and its brokerage subsidiary, NationsBanc Securities, Inc. (collectively, NationsBank), for permission for the subsidiary to act as an agent in the sale of a variety of fixed and variable annuity contracts. Although annuities come in many forms, in general they are contracts under which the purchaser makes one or more premium payments to the issuer, in return for the right to receive a series of periodic payments, which continue either for a fixed period or for the life of the purchaser or a designated beneficiary. See generally D. Shapiro & T. Streiff, *Annuities* 2-4 (1992) (hereafter *Annuities*). The annuity contracts that NationsBank proposed to sell were "designed to provide investors with the opportunity to invest and accumulate capital on a tax-deferred basis, for retirement or other long-term goals." Pet. App. 35a.

"Immediate" annuities begin making periodic payments shortly after the contract is purchased, and are primarily a mechanism for structuring the investment of a given capital sum and its repayment on a level-payment, self-amortizing basis.[2] See *Annuities* 3.

---

[2] That is, the amount of each periodic payment is fixed, and is calculated so that over the agreed or actuarially predicted payout period the purchaser will receive back an amount equal to the total premium paid, less applicable expenses and fees, plus interest at a predetermined rate. As explained below, modern annuities often guarantee a minimum fixed payment amount, but provide that the issuer may increase payments, in

Most annuities sold in the modern market, however, are "deferred" annuities. *Id.* at 4. Deferred annuities involve an initial "accumulation period," during which the purchaser's payments are held and invested by the issuer, and interest or investment returns are periodically credited to the purchaser's account. See *id.* at 3. At the end of the accumulation period the purchaser generally has the right to select one of a number of options for repayment of the account's accumulated value, including lump-sum distribution, systematic withdrawals, or the purchase of an "immediate" annuity (generally at rates specified in the original contract). *Id.* at 4.

Annuities are commonly described as either "fixed" or "variable." Those terms refer to the terms on which the annuity issuer promises to hold and repay the purchaser's investment. The issuer of a fixed annuity promises that the purchaser's investment will earn interest (during both the accumulation and the payout phase) at a modest guaranteed rate. In addition, most modern "fixed" annuities (including all those at issue in this case) also provide for the potential payment of "excess" interest, at the issuer's discretion and at whatever rate it may set from time to time (although a particular "excess" rate may be guaranteed for some period after inception of the contract). See Pet. App. 36a-37a & n.1; see generally *Annuities* 34-36, 41-42 & illus. 5.1; *Associates in Adolescent Psychiatry, S.C.* v. *Home Life Ins. Co.*, 941, F.2d 561, 564-568 (7th Cir. 1991) (discussing securities law consequences of particular "excess interest" structure), cert. denied, 112 S. Ct. 1182

---

its discretion, on the basis of favorable overall investment experience.

(1992). Thus, the purchaser of a deferred fixed annuity relinquishes control over the invested premium and receives, in return, a general obligation of the issuer, backed by its overall credit and assets, that promises repayment of principal, a modest guaranteed return, and the possibility of greater returns based on the issuer's investment experience. See Pet. App. 36a; see also *Annuities* 39-40, 69-70.

In a "variable" annuity, on the other hand, the issuer typically promises to segregate premiums received from the purchaser into a separate account and to invest them in one or more of a number of possible investments—such as a group of mutual funds—as directed by the purchaser. The value of a deferred variable annuity during or at the end of the accumulation period is determined largely by the performance of the selected investments, although the issuer may guarantee preservation of principal or a modest minimum rate of return. Thus, the purchaser retains both substantial investment control and the associated risk of gain or loss. See generally Pet. App. 35a-36a; *Annuities* 5, 49, 51; Office of the Comptroller of the Currency (OCC), Interpretive Letter No. 499, [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,090 at 71,211 (Feb. 12, 1990) (OCC Ltr. No. 499) (describing annuities involved in this case). A deferred annuity may be variable only during the accumulation period, or may continue to provide variable returns if the contract provides for (or the purchaser chooses) a variable annuity payout option. Compare, *e.g.*, *SEC* v. *United Benefit Life Ins. Co.*, 387 U.S. 202, 205-206 (1967), with *SEC* v. *Variable Annuity Life Ins. Co.*, 359 U.S. 65, 69-72 & n.13 (1959).

Both fixed and variable annuities are covered by an unique and complex set of federal income tax rules that generally allow for deferral of tax on the investment returns allocable to a purchaser's annuity payments until those returns are withdrawn during the payout phase of the contract. See 26 U.S.C. 72; *Annuities* 70-73. Because the tax rules also generally provide for penalties if an annuity investment is withdrawn before the purchaser is 59½ years old, and for unfavorable tax treatment of amounts withdrawn before the maturity of the contract, annuities are frequently marketed as a tax-sheltered means of saving for retirement. See *Annuities* 7, 83-85, 107-108; 26 U.S.C. 72(e) and (q); Pet. App. 38a.

2. NationsBank sought approval from the Comptroller of the Currency for its proposal to act as a sales agent for (not as issuer of) a variety of annuity contracts that would allow purchasers to design "a flexible, multi-faceted investment package comprised of variable and fixed annuity options." Pet. App. 37a. The OCC Chief Counsel's interpretive letter underlying the Comptroller's approval of NationsBank's proposal (see *id.* at 35a) noted that the OCC had previously reached the conclusion that national banks have the authority to sell variable annuities, on the ground that "variable annuity contracts are securities, functionally resembling shares in a mutual fund, and * * * banks are authorized, pursuant to 12 U.S.C. § 24(7) to buy and sell securities for the account of customers." OCC Ltr. No. 499 at 71,211, citing OCC, Interpretive Letter No. 331, [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,501 (Apr. 4, 1985) (OCC Ltr. No. 331).[3] The

[3] The second sentence of 12 U.S.C. 24 Seventh (added by Section 16 of the Banking Act of 1933 (Glass-Steagall Act),

Comptroller adopted (Pet. App. 37a) the Chief Counsel's view that insofar as the annuities involved in NationsBank's proposal were "securities" within the meaning of 12 U.S.C. 24 Seventh, they would fall within the scope of that prior determination. The additional analysis provided by the Chief Counsel's letter and the Comptroller's approval in this case therefore focused on NationsBank's proposal to market fixed annuities, although the approval extended to the entire range of annuity products described in the bank's application.[4]

The statutory grant of power to national banks, 12 U.S.C. 24 Seventh, provides that such banks may

---

Act of June 16, 1933, ch. 89, § 16, 48 Stat. 184) refers expressly to the "business of dealing in securities and stock" by a national bank, but limits that business "to purchasing and selling such securities without recourse, solely upon the order, and for the account of, customers, and in no case for its own account," and provides that banks "shall not underwrite any issue of securities or stock." OCC Ltr. No. 331 concluded (at 77,774) that because variable annuities are similar to shares in a mutual fund, they should be considered "securities" within the meaning of that provision, and therefore within the power of national banks to sell "solely upon the order, and for the account of, customers." Compare *SEC* v. *Variable Annuity Life Ins. Co.*, 359 U.S. at 71-72 (variable annuities are "securities" subject to the registration requirements of the Securities Act of 1933); *SEC* v. *United Benefit Life Ins. Co.*, 387 U.S. at 210-211 (1967) (same as to variable accumulation period of contract with fixed annuity payout option).

[4] The Comptroller determined (Pet. App. 37a-38a) that sales of fixed annuities were permissible even if such annuities were not "securities" for purposes of 12 U.S.C. 24 Seventh (see note 3, *supra*). He therefore had no occasion to consider the question whether fixed annuities are "securities," and that question is not presented in this case.

exercise "all such incidental powers as shall be necessary to carry on the business of banking." In applying that general provision to NationsBank's application, the Comptroller stated that "[a]s part of their traditional role as financial intermediaries, [national] banks have broad powers to buy and sell financial investment instruments as agent for customers." Pet. App. 38a. He noted that "[a]lthough annuities have historically been a product of insurance companies, they are primarily financial investments," because annuity purchasers "are not seeking to pool a catastrophic risk such as death, injury, or property damage, but are instead seeking a guaranteed, long-term return on their assets." *Ibid.* The opinion acknowledged the element of "mortality risk" present in some annuities, but concluded (in accordance with a number of authorities) that it "is essentially an investment risk, not an insurance risk," and that "although annuities often share with insurance the need for actuarial calculations, they are primarily a vehicle for investment." *Id.* at 38a-39a.

Further, the Comptroller found a "close functional resemblance between fixed annuity contracts and other financial investment instruments that banks may sell as agent" (Pet. App. 39a), including variable annuities, conventional debt instruments, and certificates of deposit. *Id.* at 39a-41a. Indeed, "[t]he financial marketplace provides many examples of instruments that, like fixed annuities, pay the investor a fixed stream of income over time in return for an initial investment." *Id.* at 41a. The Comptroller therefore concluded that "fixed annuity contracts are financial investment instruments that national banks have authority to sell as agent." *Ibid.*

The Comptroller next considered (Pet. App. 41a-47a) whether 12 U.S.C. 92 (Supp. V 1993), which permits national banks in towns of 5,000 or fewer inhabitants to "act as the agent for any fire, life, or other insurance company * * * by soliciting and selling insurance and collecting premiums," by implication prohibits national banks in larger towns and cities from selling annuities. He first noted the OCC's traditional position that Section 92, which grants small-town banks general insurance agency powers "in addition" to their other powers as national banks, was intended only to provide such banks with an additional source of revenue, and implies no restriction on the powers conferred by Section 24 Seventh on all national banks, wherever located. Pet. App. 42a. Moreover, after reviewing available authorities (*id.* at 43a-47a), the Comptroller concluded that because annuities are "primarily a vehicle for investment" (*id.* at 45a) and "lack the basic insurance characteristic of indemnification against risk" (*id.* at 47a), they should not in any event be considered "insurance" for purposes of Section 92. Pet. App. 47a.

The Comptroller also pointed out (Pet. App. 42a-43a) that Section 92 speaks only of a bank's power to act as an agent for any "fire, life, or other insurance company." Applying the principle of "ejusdem generis," he concluded that the statute should be read to apply only to "types of insurance that are similar to fire and life insurance, such as other general casualty insurance policies." Pet. App. 43a. Thus, even if annuities were to be considered "insurance" for purposes of Section 92, they would remain "a specialized product, unrelated to the gen-

eral life and casualty policies that section 92 concerns." Pet. App. 43a. That Section would therefore have no application to annuities, which should be analyzed only to determine whether their sale was part of or incidental to "the business of banking" under 12 U.S.C. 24 Seventh. Pet. App. 43a.

Finally, the Comptroller determined (Pet. App. 47a-48a) that there were no policy or supervisory issues that counselled against permitting NationsBank to make agency sales of annuities. On the contrary, he noted that such sales would provide "a logical complement to other financial services offered by [NationsBank], such as investment advice and discount brokerage services," would provide additional income for the banks, and would help the bank "compete effectively with other providers of financial services." *Ibid.* Customers would also benefit from the increased range of products made available to them through the bank. *Ibid.* Because the bank would act only as agent, it would incur no interest rate or actuarial risks. *Id.* at 48a. Finally, in order to eliminate any risk of customer confusion, the Comptroller required that NationsBank "expressly disclose in its advertising and promotional materials, and * * * when describing the [annuities] to customers, that the [annuities] are not products of [NationsBank] and are not FDIC insured," and obtain a signed statement from each annuity purchaser acknowledging the bank's agency status and the lack of federal insurance. *Ibid.* On those conditions, the Comptroller permitted NationsBank to proceed with agency sales of annuities.

3. Respondent Variable Annuity Life Insurance Company, an issuer of annuities, filed suit in federal district court to overturn the Comptroller's approval.

The district court granted summary judgment for the Comptroller. Pet. App. 29a-34a. Addressing primarily respondent's argument under 12 U.S.C. 92, the court found it "neither arbitrary nor capricious" to view that Section "as a supplemental powers provision and not a limitation on national banks['] incidental powers under § 24(7)." Pet. App. 33a-34a. Moreover, applying the principles articulated in *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), the court deferred to the Comptroller's "reasonable interpretation" that "annuities are primarily financial investment instruments, not insurance" for purposes of the relevant banking laws. Pet. App. 33a. Finally, the court upheld as reasonable the Comptroller's determination that "annuities are a specialized product," unlike the general life and casualty insurance covered by Section 92. Pet. App. 34a.

The court of appeals reversed. Pet. App. 1a-17a. Relying in substantial part on its decision in *Saxon* v. *Georgia Ass'n of Indep. Ins. Agents*, 399 F.2d 1010 (5th Cir. 1968), the court determined that 12 U.S.C. 92 imposes an affirmative limitation on the power of national banks not located in small towns to sell any form of "insurance." Pet. App. 6a-10a, 15a-17a. The court then rejected the Comptroller's conclusions that annuities are not "insurance" for purposes of Section 92 (Pet. App. 10a-13a) and that, in any event, the statute applies only to general forms of insurance akin to fire and life insurance (*id.* at 13a-14a).

The court read the legislative history of Section 92 to indicate that the general banking authority conferred by 12 U.S.C. 24 Seventh "did not grant banks the power to sell insurance products." Pet.

App. 16a-17a. The court remarked in passing (*id.* at 15a) that even if agency sales of annuities were "incidental" to the "business of banking," the power to make them could not be deemed "necessary" to carrying on that business under Section 24 Seventh's general grant of "all such incidental powers as shall be necessary to carry on the business of banking." In any event, the court held that even if Section 24 Seventh, read alone, would authorize banks to sell annuities, the specific limitations that the court found in Section 92 would supersede anything to the contrary in the more general statute. Pet. App. 15a-16a.

The full court of appeals rejected petitioners' suggestions of rehearing en banc, with six judges recused and four dissenting. Pet. App. 18a-19a. The four dissenters observed that "Section 92 nowhere defines 'insurance,'" and reasoned that "[u]nder *Chevron*, this should leave it to the Comptroller to arrive at a reasonable definition, insofar as [the statute] relates to the industry within his jurisdiction." *Id.* at 24a. Their opinion reviewed a number of relevant authorities (*id.* at 24a-27a) and concluded that on the question whether annuities are "insurance" for purposes of Section 92, "[t]he better view—and certainly a reasonable one that is entitled to deference under *Chevron*—is that of the Comptroller." Pet. App. 24a.

INTRODUCTION AND SUMMARY OF ARGUMENT

The Comptroller of the Currency has been charged by Congress with the oversight and regulation of national banks. See generally 12 U.S.C. 1, 26-27, 481; *Investment Co. Inst.* v. *Camp*, 401 U.S. 617, 626-627 (1971). In this case, the Comptroller deter-

mined that federal law permits such banks to act as agencies in the sale of annuities to their customers, because the power to conduct such sales is "incidental" to the "business of banking" under 12 U.S.C. 24 Seventh. That determination rests in large part on the Comptroller's conclusion that the annuities in question are functionally investment instruments for purposes of the federal banking laws, whether or not they are also "securities" that banks are expressly permitted to broker under Section 24 Seventh. National banks have traditionally served as intermediaries for their customers in the purchase and sale of financial investments. If annuities are investments, then acting as an agent for their sale is certainly part of, or incidental to, the business of banking.

The court of appeals overturned the Comptroller's decision in this case on the basis of two conclusions of its own: that annuities should be considered forms of "insurance" for purposes of 12 U.S.C. 92 (Supp. V 1993), and that Section 92 prohibits banks located outside small towns from acting as sales agents for any "insurance" product, even if the Comptroller has determined that sales of that product are incidental to the "business of banking." Both those conclusions are erroneous. Dictionary definitions, functional analysis and relevant authorities all indicate that annuity products are distinctly different from policies of insurance: instead of focusing on indemnification from risk of loss, they focus largely or even exclusively on investment management and the return of principal and investment income over time. Moreover, the language of Section 92 indicates that it is a grant of additional authority to national banks located in small towns to act as agents for the full

range of life and casualty insurance products, without regard to the relationship of those products to the business of banking; there is no reason to read it more broadly to prohibit national banks located in other places from acting as agents in the sale of particular "insurance" products when the Comptroller has specifically determined that such sales are properly incidental to the banks' business within the meaning of the general grant of authority found in 12 U.S.C. 24 Seventh.

In any event, the Comptroller's resolution of each of the questions of statutory interpretation involved in this case is clearly reasonable, and reflects the application of his specialized knowledge and policy judgment. The court of appeals erred in substituting its judgment for that of the Comptroller in an important area entrusted by Congress to the Comptroller's administrative oversight and regulation. *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-845 (1984); *Clarke* v. *Securities Indus. Ass'n*, 479 U.S. 388, 403-404 (1987); *Investment Co. Inst.* v. *Camp*, *supra*.

ARGUMENT

I. ACTING AS AN INTERMEDIARY WITH RESPECT TO CUSTOMERS' FINANCIAL INVESTMENTS FALLS WITHIN A NATIONAL BANK'S STATUTORY AUTHORITY TO EXERCISE "ALL SUCH INCIDENTAL POWERS AS SHALL BE NECESSARY TO CARRY ON THE BUSINESS OF BANKING"

A. Federal Law Grants National Banks Broad And Flexible Authority To Carry On The Business Of Banking

The first sentence of 12 U.S.C. 24 Seventh authorizes national banks

> [t]o exercise * * * all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of title 62 of the Revised Statutes.

That provision originated in Section 11 of the 1863 statute that first established the national banking system. Act of Feb. 25, 1863, ch. 58, § 11, 12 Stat. 668. Section 11 granted national banks the power

> to carry on the business of banking by obtaining and issuing circulating notes * * *; by discounting bills, notes, and other evidences of debt; by receiving deposits; by buying and selling gold and silver bullion, foreign coins, and bills of exchange; by loaning money on real and personal security * * *, and by exercising such incidental

> powers as shall be necessary to carry on such business[.]

The language, purpose, and original structure of the statute all indicate that Congress intended both to enumerate certain core banking activities, and also to leave ample scope for the exercise of other, unenumerated powers that might be or become part of or "incidental" to carrying on the business of banking.[5]

Section 11 of the 1863 Act was modeled on Section 18 of New York's Free Banking Law of 1838, ch. 260, 1838 N.Y. Laws 249. See Cong. Globe, 37th Cong., 3d Sess. 1114 (1863) (remarks of Rep. Spaulding); Bray Hammond, *Sovereignty and an Empty Purse: Banks and Politics in the Civil War* 160 (1970). That fact is significant because, at the time Congress passed the 1863 Act, New York's highest court had made clear that the state statute was to be broadly interpreted. In *Curtis* v. *Leavitt*, 15 N.Y. 9 (1857), the state Court of Appeals upheld the power of banks chartered under the Free Banking Law to borrow money in the course of their business, even though the statute did not specifically

---

[5] One year after Section 11's initial passage, Congress changed its language to substantially the form it takes today. See Act of June 3, 1864, ch. 106, § 8, 13 Stat. 99, 101. There is no indication that Congress intended the 1864 consolidation of the statute's references to "carry[ing] on the business of banking" and "exercising * * * incidental powers" into one introductory clause to effect any substantive change in the authority conferred by the statute. See Symons, *The "Business of Banking" in Historical Perspective*, 51 Geo. Wash. L. Rev. 676, 700 (1983). Indeed, because the object of the 1864 Act was to encourage state banks to convert to national charters, it would have been counterproductive to use it to narrow the scope of national bank authority. *Ibid.*

grant any such power. One judge explained that the statutory specifications were not intended "to restrict the appropriate business of banking," *id.* at 58 (Comstock, J.), while another observed that the "implied powers" granted by the statute were "not enumerated and defined; because no human sagacity can foresee what implied powers may, [with] the progress of time, the discovery and perfection of better methods of business, and the ever-varying attitude of human relations, be required to give effect to the express powers." *Id.* at 157 (Brown, J.).[6]

Similarly, this Court has long allowed national banks considerable flexibility in exercising, under the Comptroller's supervision, the authority granted by Section 24 Seventh. Thus, national banks have been permitted to certify checks, *Merchants' Bank* v. *State Bank*, 77 U.S. (10 Wall.) 604 (1871); purchase securities in the course of settling a claim, *First Nat'l Bank of Charlotte* v. *National Exch. Bank*, 92 U.S. 122 (1876); pay state taxes on depositors' accounts, *Clement Nat'l Bank* v. *Vermont*, 231 U.S. 120 (1913); operate a safe deposit business, *Colorado Nat'l Bank* v. *Bedford*, 310 U.S. 41 (1940); and engage in advertising, *Franklin Nat'l Bank* v. *New York*, 347 U.S. 373 (1954), although none of those activities is specifically mentioned in Section 24 Seventh.[7]

---

[6] It is reasonable to assume that Congress was aware of the decision in *Curtis* when it passed the federal bank powers provision six years later. *Arnold Tours, Inc.* v. *Camp*, 472 F.2d 427, 431 (1st Cir. 1972). Two of the three members of the House subcommittee that originated the federal statute—including Elbridge Spaulding, its principal draftsman—were New York bankers. Hammond, *supra*, at 159-160.

[7] This Court's decisions have adopted a pragmatic approach to the scope of bank powers. Thus, the Court has considered

Recent cases in the lower courts have continued to recognize that, because the banking business is continually changing and evolving, the powers of national banks "must be construed so as to permit the use of new ways of conducting the very old business of banking." *M & M Leasing Corp.* v. *Seattle First Nat'l Bank*, 563 F.2d 1377, 1382 (9th Cir. 1977), cert. denied, 436 U.S. 956 (1978) (power to enter into financing arrangements structured as leases); see also *First Nat'l Bank of E. Ark.* v. *Taylor*, 907 F.2d 775, 778 (8th Cir.), cert. denied, 498 U.S. 972 (1990) (debt cancellation contracts); *Securities Indus. Ass'n* v. *Clarke*, 885 F.2d 1034, 1049 (2d Cir. 1989), cert. denied, 493 U.S. 1070 (1990) (issuance of mortgage pass-through certificates); *American Ins. Ass'n* v. *Clarke*, 865 F.2d 278, 281-282 (D.C. Cir. 1988) (provision of municipal bond "insurance"); *Dyer* v. *Broadway Central Bank*, 169 N.E. 635, 636 (N.Y. 1930) ("care should be exercised not to cripple [banks] and break down their usefulness by a narrow and unreasonable construction of the statutes which will result in unwisely limiting their usefulness in the transaction of business under modern conditions."). And the New York Court of Appeals has recently reaffirmed, in upholding the authority

---

it relevant that an activity "has grown out of the business needs of the country," *Merchants' Bank*, 77 U.S. (10 Wall.) at 648; that it is a "reasonable and appropriate measur[e] * * * to meet all the legitimate demands of the authorized business," *First Nat'l Bank of Charlotte*, 92 U.S. at 127; that it would "promote the convenience of [the] business," *Clement Nat'l Bank*, 231 U.S. at 140; that it is a "generally adopted method" of banking, *Colorado Nat'l Bank*, 310 U.S. at 50; or that "[m]odern competition for business finds [it] one of the most usual and useful of weapons," *Franklin Nat'l Bank*, 347 U.S. at 377.

of New York banks to sell fixed and variable annuities under state law, its longstanding broad construction of the statute that provided the original pattern for Section 24 Seventh: "We have long been mindful that the business of banking is not static but rather must adjust to meet the needs of the customers to whom banking organizations provide a useful service." *New York State Ass'n of Life Underwriters* v. *New York State Banking Dep't*, 632 N.E.2d 876, 880 (1994).

B. Acting As An Intermediary In Customers' Investment Transactions Is Traditionally Part Of Or Incidental To The Business Of Banking

1. Brokerage of financial instruments, such as securities, has long been a customary part of the business of banking. Indeed, Congress acknowledged the power of national banks to engage in securities brokerage in Section 2 of the McFadden Act, Act of Feb. 27, 1927, ch. 191, 44 Stat. 1226, and Section 16 of the Glass-Steagall Act, Act of June 16, 1933, ch. 89, § 16, 48 Stat. 184. The McFadden Act explicitly authorized banks to engage in "the business of buying and selling securities"; the Glass-Steagall Act, a few years later, limited banks' "business of dealing in securities and stock" to purchasing and selling securities "solely upon the order, and for the account of, customers." 12 U.S.C. 24 Seventh. Neither Act created the authority for banks to broker securities; each merely recognized and regulated that authority, which stems instead from Section 24 Seventh's general grant of power to banks to "exercise all such incidental powers as shall be necessary to carry on the business of banking." See *Clarke* v. *Securities Indus. Ass'n*, 479 U.S. 388, 407-408 & nn.20-22

(1987) (before McFadden Act, banks conducted securities transactions "on a widespread * * * basis"); *Securities Indus. Ass'n* v. *Board of Governors*, 468 U.S. 207, 215 (1984) ("[b]anks long have arranged the purchase and sale of securities as an accommodation to their customers"; Glass-Steagall "expressly endorsed" that "traditional banking service").

The authority of national banks to broker investment instruments for customers is not limited to instruments that are "securities" within the meaning of Section 24 Seventh and the Glass-Steagall Act. The Comptroller has explained that brokerage of investment instruments is generally within the "business of banking," because of the financial aspects of such brokerage and its relationship to other traditional banking functions:

> National banks possess various express or implied powers to invest in, trade, deal in, underwrite, and otherwise act in various capacities with a wide variety of financial, investment, and monetary instruments and other financial commodities (such as exchange, coin, and bullion). Banks are regular, active participants in the financial trading markets and normally will have trading expertise. It is a natural part of the same trading process for banks to serve as broker[s] for their customers in other transactions where the bank could not or does not serve as principal but where the trading activity is essentially similar.

OCC, Interpretive Letter No. 494, [1989-1990 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 83,083, at 71,199 (Dec. 20, 1989) (OCC Ltr. No. 494). The Comptroller has accordingly permitted national banks to broker various other types of investment instru-

ments on behalf of their customers, whether or not particular instruments would be considered "securities" for purposes of Section 24 Seventh.[8] Thus, once the Comptroller had analyzed the characteristics of the annuities that NationsBank proposed to market and determined, as discussed below, that they were essentially investment instruments, it was reasonable for him to conclude that agency sales of such annuities fell well within the scope of national banks' traditional activities in brokering investment instruments for their customers.

2. The court of appeals suggested in passing (Pet. App. 15a) that Section 24 Seventh does not authorize agency sales of annuities, because the power to make such sales is neither "incidental" nor "necessary" to the "business of banking." Assuming that the court's brief remark to that effect should be regarded as an independent holding, it is incorrect. First, in light of

---

[8] See OCC Ltr. No. 494 at 71,199-71,200 & n.4 (commodities futures and related options); OCC Letter No. 387, [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,611 (June 22, 1987) (real estate loans); OCC Letter No. 365, [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,535 (Aug. 1, 1986) (financial futures); OCC Letter No. 357, [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,527 (Feb. 26, 1986) (options on financial instruments and on financial futures); OCC Letter No. 356, [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,526 (Jan. 7, 1986) (agricultural and metal futures used for hedging); OCC Letter No. 326, [1985-1987 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,496 (Jan. 17, 1985) (options); OCC Letter No. 271, [1983-1984 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,435 (Sept. 21, 1983) (real estate loans and equity interests).

the history discussed above, the language of Section 24 Seventh explicitly recognizing banks' "business of dealing in securities and stock," and banks' "traditional role as financial intermediaries" (Pet. App. 38a), it is implausible to contend that brokering investment instruments on behalf of customers is not "incidental" to the traditional, let alone the contemporary, business of banking.

Second, the suggestion that the power to engage in activities that are properly part of or incidental to the banking business should be restricted by some narrow concept of what is "necessary" cannot be reconciled with the well-established proposition that the statutory term "necessary" need not mean "indispensable." As this Court recognized long ago, particularly when used to define general powers available to meet changing and unforeseeable future circumstances, the term need mean no more than convenient or useful. *M'Culloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316, 413-415 (1819); see also *National R.R. Passenger Corp.* v. *Boston & Maine Corp.*, 112 S. Ct. 1394, 1402 (1992); *Black's Law Dictionary* 1029 (6th ed. 1990); *Curtis* v. *Leavitt*, 15 N.Y. at 64 (Comstock, J.); *New York State Ass'n of Life Underwriters*, 632 N.E.2d at 880; *M & M Leasing*, 563 F.2d at 1382. Moreover, even if the meaning of the word "necessary" in Section 24 Seventh might, at one time, have been open to question, that question has long been settled by the Comptroller, to whom Congress has entrusted the statute's administration. Both the Comptroller's view on that issue and his further determination of what "incidental powers" are "necessary" to allow national banks to conduct

their business are permissible constructions of the statute, and are entitled to deference. *National R.R. Passenger Corp.*, 112 S. Ct. at 1402.

II. THE COMPTROLLER REASONABLY DETERMINED THAT THE SALE OF ANNUITIES BY NATIONAL BANKS IS NOT PROHIBITED BY 12 U.S.C. 92

In rejecting the Comptroller's decision in this case the court of appeals relied primarily on its conclusion that bank sales of annuities, whether or not otherwise authorized under 12 U.S.C. 24 Seventh, are independently prohibited by 12 U.S.C. 92. Section 92 provides:

> In addition to the powers now vested by law in national banking associations * * *[,] any such association located and doing business in any place the population of which does not exceed five thousand inhabitants * * * may, under such rules and regulations as may be prescribed by the Comptroller of the Currency, act as the agent for any fire, life, or other insurance company * * * by soliciting and selling insurance and collecting premiums on policies issued by such company.

The Comptroller, on the other hand, determined that annuities are not "insurance" within the meaning of Section 92 (Pet. App. 43a-47a); and that, even if they were, Section 92 should not be read to limit their sale, particularly if such sales would be incidental to the business of banking under Section 24 Seventh. Pet. App. 41a-43a.

Section 92 itself neither defines the term "insurance" nor specifies whether its supplemental grant of authority is meant to limit the powers of national

banks not located in small communities. As the district court (and the dissenters from denial of rehearing en banc) recognized (Pet. App. 33a, 24a), those interpretive questions are for the Comptroller to answer, so long as his interpretations are reasonable. *E.g.*, *Chevron*, 467 U.S. at 843; see also *Clarke* v. *Securities Indus. Ass'n*, 479 U.S. at 403-404. The Comptroller's conclusions in this case were reasonable, and the court of appeals erred in failing to defer to his construction of the statute.

A. The Comptroller Reasonably Determined That Annuities Are Not "Insurance" For Purposes Of Section 92

1. As the Comptroller's approval in this case explained, "[d]ictionary definitions of 'insurance' invariably describe it as a contract for indemnification against risk of loss." Pet. App. 43a-44a (citing examples). *Black's Law Dictionary* (6th ed. 1990), for example, defines "insurance" in part as "[a] contract whereby, for a stipulated consideration, one party undertakes to compensate the other for loss on a specified subject by specified perils," or "undertakes to indemnify another against loss, damage, or liability arising from an unknown or contingent event." *Id.* at 802. *Webster's Third New International Dictionary* (1986) includes similar definitions: "a device for the elimination or reduction of an economic risk common to all members of a large group and employing a system of equitable contributions out of which losses are paid"; "coverage by contract whereby for a stipulated consideration one party undertakes to indemnify or guarantee another against loss by a specified contingency or peril." *Id.* at 1173.

Definitions of the term "annuity," on the other hand, emphasize (as the term itself suggests) the periodicity of payments and their character as investment returns. Thus, *Black's Law Dictionary* describes an annuity (at 90) as "[a] right to receive fixed, periodic payments, either for life or for a term of years" or "[a] fixed sum payable to a person at specified intervals for a specific period of time or for life," and notes specifically that "[p]ayments represent a partial return of capital and a return (interest) on the capital investment." According to *Webster's* (at 88), the term means "an amount payable yearly or at other regular intervals (as quarterly) for a certain or uncertain period (as for years, for life, or in perpetuity)," or "a contract or agreement under which one or more persons receive annuities in return for prior set payments made by themselves or another (as an employer)." [9]

The difference in dictionary definitions reflects a difference in commercial and financial reality. In his decision in this case, the Comptroller first considered

---

[9] The court of appeals cited (Pet. App. 10a) the reference to "annuity insurance" in the seven-page catalogue of descriptive "classifications" following the definition of "insurance" in *Black's Law Dictionary* (at 802). Although its meaning is not entirely clear, that reference appears to describe a particular type of insurance policy, the proceeds of which would be paid out as an annuity, rather than in a lump sum. That is, it seems likely that the description of "annuity insurance" is not meant to define the word "annuity," any more than the immediately following description of "assessment insurance" is intended to define the word "assessment." The definition of "annuity" (like the definition of "assessment") is located where one would expect it—under "A." See *id.* at 90; compare the descriptions of various types of annuities following the primary definition.

the functional nature of the annuity products in question, and concluded that they are "primarily financial investments." Pet. App. 38a. As the decision noted (*ibid.*), investors who purchase fixed annuities generally "are not seeking to pool a catastrophic risk such as death, injury or property damage, but are instead seeking a guaranteed, long-term return on their assets."[10] Indeed, "[m]ost commonly, annuities are marketed as a tax-sheltered means of saving for retirement." *Ibid.*

During the accumulation period, annuities bear a close functional resemblance to other investment products that banks would be allowed to purchase or sell on behalf of customers: mutual fund shares in the case of variable annuities (under which the purchaser retains significant investment control and risk), and conventional interest-bearing debt in the case of fixed annuities.[11] See Pet. App. 39a-41a; see

---

[10] The amount of the return (or of principal) that is "guaranteed" may vary considerably from contract to contract. See generally pages 4-6, *supra*.

[11] As explained above (see pages 7-8 & n.3, *supra*), the OCC's legal staff some years ago reached the conclusion that national banks are permitted to broker variable annuities, on the ground that variable annuities resemble mutual fund shares and are "securities" for purposes of 12 U.S.C. 24 Seventh's explicit reference to banks' "business of dealing in securities." The Comptroller's decision in this case restated that conclusion as to variable annuities, and then proceeded to uphold the sale of fixed annuities on the broader ground that even if fixed annuities are not "securities" for purposes of Section 24 Seventh, they are "financial investment interests" that banks may buy and sell on behalf of customers as part of their "traditional role as financial intermediaries." Pet. App. 38a. The judicial opinions below in this case do not distinguish in their analysis between fixed and variable an-

also *New York State Ass'n of Life Underwriters* v. *New York State Banking Dep't*, 632 N.E.2d at 882. Many modern annuity products provide for single or staged investments, an interest rate that is known or predictable at the beginning of each accumulation period, and lump-sum withdrawals during or at the end of each period or at maturity of the entire contract. Others provide for single investments, a known or predictable interest rate, and a guaranteed payout over a set term of years. Annuities with such features are virtually indistinguishable from certificates of deposit (alhough without federal deposit insurance) or conventional debt. See generally, *e.g.*, *Annuities* 19-22, 44-45.[12] At the same time, some modern

---

nuity products. In our view, the Comptroller's rationale for approving the sale of fixed annuities applies *a fortiori* to sales of variable annuities, which are even more clearly investment-oriented products; indeed, a primary rationale for the prior staff opinion was that variable annuities are primarily investment instruments. See OCC Ltr. No. 331, at 77,774, 77,776. Alternatively, the Comptroller's decision in this case adopts the legal staff's prior conclusion concerning variable annuities. Pet. App. 35a, 37a-38a; OCC Ltr. No. 499; cf. *SEC* v. *Chenery Corp.*, 318 U.S. 80, 95 (1943) (agency decision may be upheld only on grounds relied upon by agency). That conclusion is also sound on its own terms (set out in OCC Ltr. No. 331), and the Comptroller's decision to adopt it is entitled to deference.

[12] "As annuity providers became more sophisticated in their marketing efforts, they began to design products that more closely resembled those of the competition. As an annuity was a safe place to invest money at a fixed return, the bank certificate of deposit became the target competition. These products have become known as *certificate* or *CD annuities*. * * * [T]hese products have met with outstanding success[.] * * * A certificate annuity is any product where the initial interest rate guarantee period precisely parallels the surrender charge

debt instruments involve mortality risks or other contingencies that may significantly affect the interest rate, the time at which repayment is required, or the amount of principal that must be repaid. See generally, *e.g.*, Note, *Reverse Annuity Mortgages and the Due-on-Sale Clause*, 32 Stan. L. Rev. 143, 145-151 (1979) (discussing mortgages that incorporate mortality risk); David Hariton, *The Taxation of Complex Financial Instruments*, 43 Tax L. Rev. 731, 731-732 & nn.2-7 (1988). There is therefore ample support for the Comptroller's conclusion that annuities of the type that petitioner NationsBank sought to make available for purchase by its customers are correctly characterized as investment products, rather than "insurance."

2. The only feature that may lend some annuities a flavor of insurance is the mortality risk assumed by one or both parties under some annuity contracts. Under the terms of a classic single-premium, immediate-payout fixed annuity (*i.e.*, one that provides immediate income, with no accumulation period during which income is deferred), the issuer agrees to make level periodic payments throughout (but not beyond) the life of the purchaser, and the amount of each payment is calculated so as to amortize the amount paid by the purchaser, together with interest at an agreed rate, to zero as of the purchaser's actuarially expected date of death. If the purchaser dies before that date, he loses part of his principal investment, and the issuer realizes a mortality gain; if the purchaser lives beyond that date, he continues to receive

(or lack of surrenderability) period. * * * It is not a coincidence that this design is almost identical to a bank certificate of deposit." *Annuities* 44-45.

payments even though his principal has been exhausted, and the issuer realizes a mortality loss. The computations for and pricing of such a contract, like those of life insurance policies, depend on actuarial assumptions, and may reflect a single issuer's pooling of its mortality risks across a large group of purchasers.[13]

As this Court pointed out in holding that variable annuities are securities for purposes of the Securities Act of 1933, however, it is necessary to look beyond the "aspect of insurance" imparted by the presence of some mortality risk, and to focus on the characteristics of a particular product as they relate to a particular federal statutory scheme. *SEC* v. *Variable Annuity Life Ins. Co.*, 359 U.S. at 71. In that case, the relevant characteristic was the purchaser's assumption of substantial investment risk. *Ibid.* In this case, the relevant characteristic is the nature of the product, measured by its primary nature and purposes in the eyes of a prospective purchaser who is a customer of a national bank. From that perspective, the "insurance" aspect of any annuity contract is, as this Court said in an analogous context in *SEC* v. *Variable Annuity Life*, "apparent, not real; superficial, not substantial." *Ibid.*

---

[13] Most annuity contracts provide for payment of the full accumulated account value to a designated beneficiary in the event that the purchaser dies during the accumulation period. The risk that a purchaser may die before the issuer has been able to recover its sales, administrative and investment expenses through the spread between its investment returns and the returns credited to the purchaser's annuity account may also be thought of as a "mortality risk" from the issuer's point of view. See *Annuities* 93. That risk is one that the issuer runs by reason of its pricing and marketing strategy, however, and is at most a minor feature of the annuity contract.

While both life insurance contracts and some annuities involve actuarial assumptions and mortality risks, the two products are very different from the purchaser's point of view. The point of an actuarial mortality assumption is that it represents a fair estimate, at the time of contracting, of the expected life of the purchaser. The dominant character of a contract that involves such assumptions is therefore determined by the results, under the contract, if those expectations prove true. The purchaser of term life insurance pays a small amount in relation to the face amount of the policy, and expects to receive no payment in return. The dominant characteristic of such a contract is therefore indemnification against the risk of an unexpected occurrence. The purchaser of a classic, immediate-payout fixed annuity, on the other hand, pays a comparatively large amount for his contract, and expects to receive it all back, with interest. The dominant characteristic of that contract is therefore investment for an expected future income stream.[14]

---

[14] Under some life insurance policies a portion of each premium payment is invested and accumulates cash value over time. See, *e.g.*, *Black's Law Dictionary* 805 (6th ed. 1990) (descriptions of "universal" and "whole life" insurance); compare *id.* at 806 (description of "term insurance"). An annuity contract that requires or permits periodic investments (as opposed to payment of a single purchase price) bears some resemblance to the investment component of such insurance policies, but offers no analogue to the term life insurance component. That observation is consistent with the Comptroller's conclusion (Pet. App. 45a) that annuities are "primarily a vehicle for investment, not indemnification." Annuities and cash-value life insurance also both typically allow invested funds to compound on a federal income tax-deferred basis. The tax benefits accorded annuities do not, however,

Thus, even in the case of the classic immediate-payout, lifetime-based fixed annuity—the annuity contract with the most prominent "mortality risk" feature from the purchaser's point of view—the distinction between annuities and life insurance is quite apparent. As one court aptly put it, "annuities are not indemnities for death but are investments for life." *Corporation Comm'n* v. *Equitable Life Assur. Soc'y*, 239 P.2d 360, 362 (Ariz. 1951); see also *Helvering* v. *Le Gierse*, 312 U.S. 531, 541 (1941) (in terms of mortality risks, "annuity and insurance are opposites"); *Annuities* 7.[15] Nor do immediate-payout fixed annui-

---

depend on assimilating the annuity contract to insurance; annuities are treated as *sui generis* for federal income tax purposes. See 26 U.S.C. 72. In fact, it is interesting to note that death benefits received by beneficiaries under life insurance contracts are generally excluded from gross income for federal income tax purposes, whereas amounts received by a beneficiary under an annuity contract by reason of the death of the purchaser are, like other annuity payments, exempt only to the extent that they represent a return of the purchaser's invested capital. See generally 26 U.S.C. 72(e), 101(a); see also Rev. Rul. 79-335, 1979-2 C.B. 292, 294.

[15] "[A]n annuity is a cash contract * * * whose orientation to the insurer is primarily investment or asset management, and secondly, mortality management. That single fact differentiates the annuity from the life insurance product. Unlike a life insurance policy, where the primary objective is to provide death protection or estate protection for a deceased's survivors, the primary objectives of the annuity are *tax deferral, safety* and a *higher yield* than what can typically be found in a certificate of deposit, money market or savings account. Those objectives are used by the contract-holder to accumulate funds for retirement, create income for retirement or both." *Annuities* 7. The same source explains that "Annuities have very little mortality risk. * * * Instead, the annuity is an asset-management product, by which the insur-

ties—whether purchased on their own, or selected as a payout option after the accumulation period of a deferred fixed or variable annuity contract—represent the entire modern annuities market. Other types of annuity contract are much more common, and even less like insurance.[16] For example, many contemporary annuities (sometimes called "refund" annuities)

ance company makes its profit from the difference between what it can earn on its investments, and what it then pays out to the contract-holder in the form of interest rates credited to the contract." *Ibid.*

[16] Statistics compiled by the American Council of Life Insurance indicate that of 20,383,000 fixed annuity contracts issued by insurance companies and in force at the end of 1992, 89% were deferred annuities in the accumulation period. American Council of Life Insurance, *1993 Life Insurance Fact Book Update* 18 (1993) (ACLI *Update*). Of the remaining 11%, just over half (55%) were individual contracts—that is, either single-payment immediate annuities, or deferred annuities in the payout phase under which the owner had selected annuitized payments (rather than a lump-sum or "systematic withdrawals," as described below). The remainder were "supplementary contracts," providing annuitized payments of the death benefit on a life insurance policy, or of the accumulated value of a deferred annuity contract terminated by reason of the death of the purchaser. The figures for both individual and supplementary contracts include all types of annuitized payments—those payable for the life of the annuitant (and/or another beneficiary), those payable for life but with a guaranteed minimum term, and those payable for a specified term without regard to mortality. Thus, "classic" single-payment immediate annuities with a simple lifetime payout term would represent less than—and probably significantly less than—11% of the fixed annuities outstanding at the end of 1992. And those figures do not include another 6.6 million or more persons covered by individual or group variable annuity contracts issued by insurance companies. *Ibid.*

guarantee the return of the purchaser's principal investment (and perhaps a specified return), even if the purchaser dies during the payout phase but before the actuarially predicted time. See, *e.g.*, *Annuities* 20-22. Such provisions eliminate any mortality risk on the part of the purchaser, and severely limit the issuer's ability to pool positive and negative mortality experience over a broad group of annuities.

In addition, most deferred annuities provide the purchaser with the option to take payment in a lump sum at the end of the accumulation period; as regular payments over a fixed term of years, without reference to the life of the purchaser; or through "systematic withdrawals" flexibly arranged to meet the purchaser's needs, with any remaining principal paid to a beneficiary on the purchaser's death. See, *e.g.*, *Annuities* 4, 21-22, 24-26 & illus. 3.5, 122-123 (sample contract). Under those options the contract involves no element of mortality risk whatsoever, and does not even vaguely resemble "insurance." Moreover, even in cases where both return of the original investment and continued payment over the life of the purchaser is guaranteed, the remaining "mortality" element—the risk of unexpected longevity—might be characterized variously as "insurance" of a sort, as a contingent debt of the issuer, or as a contingent, post hoc adjustment in the guaranteed rate of return on the purchaser's investment. See *Annuities* 23 illus. 3.3 (computing effective rates of return under various payout options and assumptions).

The salient financial characteristics of annuities thus make clear that they are, as the Comptroller concluded, either wholly or overwhelmingly investment products. It is therefore not surprising that,

as the New York Court of Appeals recently observed, "the great weight of authority supports the position that annuities are not insurance." *New York State Ass'n of Life Underwriters* v. *New York State Banking Dep't*, 632 N.E.2d at 881. See also, *e.g.*, Pet. App. 38a-39a, 44a-45a and authorities there cited; *Annuities* 7 (in contrast to life insurance, "[a]nnuities * * * are primarily investment products"); 1 J. Appleman, *Insurance Law & Practice* § 84, at 295 (1981) ("Annuity contracts must * * * be recognized as investments rather than as insurance."); *In re Young*, 806 F.2d 1303, 1306 (5th Cir. 1987). The Comptroller's opinion in this case marshalled (Pet. App. 45a) numerous court decisions holding that annuities are not "insurance" for a variety of tax, bankruptcy, and other federal and state law purposes.[17]

---

[17] The Comptroller acknowledged (Pet. App. 46a) that cases construing the exemption for any "insurance or endowment policy or annuity contract or optional annuity contract" under Section 3(a)(8) of the Securities Act of 1933, 15 U.S.C. 77c(a)(8), "occasionally speak of fixed annuities as being 'insurance' rather than 'securities.'" See, *e.g.*, *SEC* v. *United Benefit Life Ins. Co.*, 387 U.S. 202 (1966); *SEC* v. *Variable Annuity Life Ins. Co.*, 359 U.S. 65 (1959); see also SEC Rule 151, 17 C.F.R. 230.151. However, as the Comptroller pointed out (Pet. App. 46a), the text of Section 3(a)(8) itself refers to both "annuity contract[s]" and "insurance * * * polic[ies]," rather than merely subsuming the former under the latter heading. Compare 26 U.S.C. 816(a) (defining "life insurance company" as "an insurance company which is engaged in the business of issuing life insurance *and* annuity contracts" (emphasis added)). In any event, as the Comptroller noted (Pet. App. 46a-47a), cases under Section 3(a)(8) interpret a different statute with different purposes, and do not control the analysis in the context of the banking statutes.

3. The court of appeals criticized the Comptroller's determination that annuities are not "insurance" for purposes of Section 92 on the ground that annuities are often issued by life insurance companies, and are typically regulated under state insurance laws. Pet. App. 10a-11a & n.2. But an annuity contract is not "insurance" simply because it has been issued by an insurance company, see *In re Howerton*, 21 B.R. 621, 623 (Bankr. N.D. Tex. 1982); and regulation of annuities under state insurance laws reflects little more than the fact that insurance companies have traditionally written a large proportion of annuity contracts. See *Daniel* v. *Life Ins. Co. of Va.*, 102 S.W.2d 256, 261 (Tex. Civ. App. 1937); compare *Rishel* v. *Pacific Mutual Life Ins. Co. of Cal.*, 78 F.2d 881, 883-884 (10th Cir. 1935) (annuity not "policy of insurance" required to be filed with Colorado Insurance Commissioner); *Chatham County Hosp. Auth.* v. *John Hancock Mut. Life Ins. Co.*, 325 F. Supp. 614, 619 (S.D. Ga. 1971) (annuities not regulated as "insurance" in Georgia in 1955). Both the court of appeals' observations beg the relevant question whether annuities are properly considered "insurance" or investment instruments for federal banking law purposes.[18] *New York State Ass'n of*

---

[18] As this Court recognized in the context of determining the treatment of variable annuities under the federal securities laws, what constitutes "insurance" within the meaning of a federal statute is a question of federal law. *SEC* v. *Variable Annuity Life Ins. Co.*, 359 U.S. at 69; cf., *e.g.*, *Dickerson* v. *New Banner Inst.*, 460 U.S. 103, 111-112 (1983) (meaning of "convicted" in federal statute was question of federal law, although offense and punishment were defined by state law); *United States* v. *Bess*, 357 U.S. 51, 55-57 (1958) (whether contract rights defined by state law constitute "property" under federal tax lien statute is a matter of federal law).

Life Underwriters, 598 N.Y.S.2d 824, 828 (App. Div. 1993), aff'd, 632 N.E.2d 876 (N.Y. 1994).

The court of appeals asked that question but reached the wrong conclusion. Pet. App. 12a-13a. The court recognized that, as discussed above (see pages 29-31, *supra*), annuities with lifetime payout terms may be thought of as the "inverse" or "mirror image" of term life insurance, in the sense that the mortality risk involved in one case is that the purchaser will live too long, while in the other case it is that he will die prematurely. Pet. App. 12a. But to say that two things are the "inverse" of each other is not to say that they are the same. As explained above, protecting against mortality risk is the primary functional and financial aspect of a life insurance contract. In the case of annuity contracts, on the other hand, protecting against such risk is typically no more than a supplemental consideration in an arrangement primarily concerned with the management and staged repayment of invested funds. It therefore makes little sense to argue that the banking laws should treat the two products as identical.

In all events, the court of appeals erred in approaching the question whether annuities should be viewed as "insurance" for purposes of Section 92 essentially *de novo*. That court should, like the district court, have confined its review to inquiring whether the Comptroller's fundamental determination that annuities are primarily investment vehicles, rather than contracts of indemnification, represented a permissible interpretation of the statute. See, *e.g.*, *Chevron*, 467 U.S. at 843-845; *Clarke* v. *Securities Indus. Ass'n*, 479 U.S. at 403-404; *Investment Co. Inst.* v. *Camp*, 401 U.S. at 626-627. As the preceding discussion demonstrates, the Comptroller's interpre-

tation was at least a reasonable one. Having failed to impeach its reasonableness in light of the language and purposes of Section 92 and the remainder of the federal banking laws, the court of appeals erred in substituting its judgment for that of the Comptroller on matters within his expertise and regulatory competence.[19]

---

[19] In its opposition to the certiorari petitions in this case, respondent contended (Br. in Opp. 12) that the Comptroller's determination is not entitled to deference because its is inconsistent with positions taken in 1978 and 1982. Even revised administrative positions are, of course, entitled to deference. *E.g., Good Samaritan Hosp.* v. *Shalala,* 113 S. Ct. 2151, 2160-2161 (1993). The letters to which respondent refers, however, "hardly establis[h] an inconsistent policy." *Thomas Jefferson Univ.* v. *Shalala,* No. 93-120 (June 24, 1994), slip op. 11-12. As we pointed out in our reply brief at the petition stage (at 3-4), the 1978 letter represents informal advice by an agency lawyer, contains no analysis supporting the views expressed, and clearly identifies its conclusions as the personal opinion of its author. See Br. in Opp. 1a-2a. Such a letter would not bind the agency or the recipient or be subject to review by the courts. See *New York Stock Exch.* v. *Bloom,* 562 F.2d 736, 741 (D.C. Cir. 1977), cert. denied, 435 U.S. 942 (1978); *American Land Title Ass'n* v. *Clarke,* 743 F. Supp. 491, 494 (W.D. Tex. 1989). It therefore cannot provide a basis for contending that the agency has changed course. *Independent Ins. Agents* v. *Ludwig,* 997 F.2d 958, 962 (D.C. Cir. 1993). The 1982 letter sets forth a similar informal opinion by a member of the OCC legal staff. See OCC Interpretive Letter No. 241, [1983-1984 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 85,405 (Mar. 26, 1982). Moreover, as explained in our reply brief (at 4-5), that letter's discussion of sales of term life insurance does not conflict with the Comptroller's decision in this case concerning annuities.

B. The Comptroller Reasonably Concluded That Section 92 Does Not Prohibit Agency Sales Of Specialized "Insurance" Products Outside Small Towns If The Comptroller Has Determined That Such Sales Are Part Of Or Incidental To The Business Of Banking

The court of appeals also erred in refusing to defer to the Comptroller's conclusion that even if annuities were to be considered "insurance" for purposes of 12 U.S.C. 92, the statute should not be construed to prohibit banks outside small towns from selling them (as agents) once the Comptroller has concluded that such sales are incidental to the business of banking.

Section 92 provides that "[*i*]*n addition to* the powers now vested by law in national banking associations," national banks in small towns may "act as the agent for any fire, life, or other insurance company" in selling insurance policies (emphasis added). The introductory phrase "in addition to" shows that Section 92 is a grant of additional powers for a special situation.[20] It does not purport to define, or confine, the scope of the other lawful "powers" whose existence it assumes and supplements. Those

---

[20] The statute's legislative history also indicates that Congress thought of Section 92 as a grant of additional powers, not a limitation on otherwise authorized activities. Senator Owen, Section 92's sponsor, described the provision as "giving some additional powers to the small banks to act as agents in insurance matters." 53 Cong. Rec. 11,002 (1916); see also *id.* at 11,001 (Comptroller's letter explaining that proposal reflected consideration of "how the powers of these small national banks might be enlarged"). See also *Independent Ins. Agents* v. *Board of Governors,* 736 F.2d 468, 477 n.6 (8th Cir. 1984) ("Congress was concerned only with providing small-town banks with an additional profit source, not with prohibiting city banks from selling insurance.").

powers, which pre-date and survive Section 92, include the general authority under Section 24 Seventh to "exercise * * * all such incidental powers as shall be necessary to carry on the business of banking." Even if annuities were "insurance" for purposes of Section 92, there would be no reason why the Comptroller could not conclude that those incidental powers extend to acting as a sales agent for limited classes of such "insurance" products whose essential investment character also brings them within the ambit of banks' traditional investment activities on behalf of their customers.[21]

To be sure, Section 92 carries some negative implication; Congress would have had little reason to grant small-town banks the power to act as general

---

[21] The court of appeals cited (Pet. App. 16a) documents written by the Comptroller and counsel to the Federal Reserve, prior to Section 92's passage, to show that Congress believed national banks had no authority to act as insurance agents before Section 92 was enacted. See 53 Cong. Rec. 11,001 (1916) (letter from Comptroller Williams to Senator Owen); Right of a National Bank To Write Insurance Through Its Officers, 2 Fed. Res. Bull. 73, 74 (1916) (letter from Board Counsel Elliot to Board Governor Hamlin). Both documents refer to insurance in broad terms. See 53 Cong. Rec. 11,001 (1916) (referring to "fire, life, etc." insurance); 2 Fed. Res. Bull. at 73 (analyzing the power of national banks to write "fire, cyclone, liability or other kinds of insurance"). Neither suggests that specific kinds of insurance agency activity that are closely connected to banking would not fall within the incidental powers of national banks. In any event, slim intimations of possible administrative or congressional understandings in 1916 form at best a "hazardous basis" for determining the meaning of a statute (12 U.S.C. 24 Seventh) passed 75 years earlier, as applied to the banking and investment world of today. See *Cippollone* v. *Liggett Group*, 112 S. Ct. 2608, 2619 (1992); *United States* v. *Price*, 361 U.S. 304, 313 (1960).

insurance agents if it had thought, in 1916, that any national bank could already do so under Section 24 Seventh. See Pet. App. 7a. But the court of appeals swept too broadly in concluding that Section 92's reference to *some* "insurance" sales necessarily implied that national banks could have no power, independent of Section 92, to sell *any* "insurance" product. Section 92 permits national banks in small communities to act as agents for any "fire, life, or other insurance company." Under the interpretational principle of *ejusdem generis*, a general term in a statutory list should be understood in light of the specific terms that surround it.[22] *E.g., Hughey* v. *United States*, 495 U.S. 411, 419 (1990); see also *Securities Indus. Ass'n* v. *Board of Governors*, 468 U.S. 207, 218 (1984); *Beecham* v. *United States*, 114 S. Ct. 1669, 1671 (1994). In accordance with that principle, the Comptroller permissibly concluded that Section 92's grant of authority—and any concomitant implication that authority was otherwise lacking—should be construed to refer only to the unrestricted operation of a general agency for fire, life, or other casualty insurance, and not to agency sales of particular "insurance" products when the Comptroller has determined that such sales fall within or are incidental to the business of banking.[23]

---

[22] Indeed, application of *ejusdem generis* is necessary to give significance to Congress's specification of "fire" and "life" insurance in Section 92. Under the court of appeals' reading of the statute those terms become unnecessary, because all types of insurance, including fire and life insurance, are encompassed in the phrase "any * * * insurance company."

[23] In its brief in opposition, respondent objected (at 9) to the Comptroller's reasoning on the ground that the words

The Comptroller's construction maintains an appropriate balance between Section 24 Seventh and Section 92. The general grant of powers in Section 24 Seventh permits banks to engage only in activities (including insurance agency activities) that are "incidental" to the "business of banking." Section 92, by contrast, grants banks located in small towns the *additional* authority to act as agents for the sale of a broader range of insurance products, *whether or not* such sales are incidental to the business of banking. That grant of additional authority does not negate the possibility that the sale of annuities, even if properly denominated as "insurance," is sufficiently related to the business of banking to come within the existing incidental powers of national banks. And the question whether such products, or any others, *are* so related is one within the expertise and competence of the Comptroller, not the courts.

* * * * *

In sum, Section 24 Seventh provides that national banks may exercise "all such incidental powers as shall be necessary to carry on the business of banking." It does not, however, define the "business of banking" or the powers that may be "incidental" thereto. Section 92 provides that national banks in small towns may act as the agent for "any fire, life,

---

"fire, life, or other" in Section 92 describe only the type of company for which a covered bank may act as agent, not the types of insurance it may sell. The statute provides, however, that covered banks may "act as the agent for any fire, life, or other insurance company * * * by soliciting and selling insurance and collecting premiums on policies issued by such company." The Comptroller could fairly read that language to limit both the types of companies and the types of "insurance" to which Congress intended the statute to apply.

or other insurance company" in the sale of insurance. Similarly, however, it does not specify to what types of "insurance" it refers. And neither provision speaks directly to the issue of whether a national bank may sell fixed and variable annuities as agent.

If "Congress has not directly addressed the precise question at issue," then "the question for the court is whether the agency's answer is based on a permissible construction of the statute." *Chevron*, 467 U.S. at 843. That construction need not be the only one those responsible for administration of the statute could have adopted, "or even the reading the court would have reached if the question initially had arisen in a judicial proceeding"; it need only be rationally permissible under the governing statute. *Id.* at 843 n.11. As demonstrated above and in the Comptroller's thorough opinion approving the application at issue here, there is ample support for the Comptroller's statutory interpretations in this case.

The regulation of banking is an area of prime importance, requiring a combination of special functional expertise and informed choices among sometimes conflicting goals. Those goals include both the maintenance of a strong banking industry in light of modern developments in investment and finance, and the protection of banks and bank customers from the expansion of bank activities into inappropriate areas. It would be difficult to identify a regulatory context in which it is clearer that courts should defer, in matters of statutory interpretation, to "reasonable accommodation[s] of conflicting policies that were committed to the agency's care by the statute." *Chevron*, 467 U.S. at 845 (quoting *United States* v. *Shimer*, 367 U.S. 374, 383 (1961)). The reasonable statutory interpretations adopted by the Comptroller

in this case were thoroughly discussed and well supported in his decision, and they are entitled to deference.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

DREW S. DAYS, III
Solicitor General

FRANK W. HUNGER
Assistant Attorney General

PAUL BENDER
Deputy Solicitor General

EDWARD C. DUMONT
Assistant to the Solicitor General

MARK B. STERN
JACOB M. LEWIS
Attorneys

JULIE L. WILLIAMS
Chief Counsel

L. ROBERT GRIFFIN
ROSA M. KOPPEL
YVONNE D. MCINTIRE
Attorneys
Office of the Comptroller of the Currency

JULY 1994

☆ U. S. GOVERNMENT PRINTING OFFICE; 1994 301157 86180